THE ECONOMIC SIGNIFICANCE OF INTERLOCKING DIRECTORATES IN RAILWAY FINANCE

It is necessary at the outset to define our terms. That very convenient and elastic word "significance" covers a multitude of considerations and permits of wide latitude in treatment. Under its shelter I shall try to analyze the various manifestations of corporate interlocking with the object of appraising their value from the economic and social standpoint. An interlocking directorate seems by its terms to denote mutual exchange of directors between associated corporations, each corporation being represented designedly on the board of the other. But if the term ever was so narrowly used, it has now been widened materially in scope. It no longer necessarily suggests the practice of exchange of representatives. Two corporations would be interlocked in their directorates were a member of one board to secure his election on another; that is, were a member of the board of Corporation A to be made a member of the board of Corporation B without B of its own volition seeking any representation on the directorate of A. By a strict use of terms these two corporations would be locked but not interlocked. I shall confine myself to "associated" corporations, for while interlocking can be said to exist whenever directorates contain the same individuals, no matter how remotely related the two corporations may be, yet such remote affiliations have no great economic significance. The essence of the relationship which I propose to discuss lies in the mutuality of interest of the connected corporations.

But we shall not reach the heart of the problem if we confine our attention to service as directors by the same individuals on boards of associated corporations. We should be regarding the mere form of things and overlooking the substance. What concerns us is the interlocking of interests in such manner as to effect a substantial influence upon the policy of both corporations. To be sure this may be most directly accomplished by the election of the same individual to both boards; but it may also be attained in

some indirect manner, as by a substantial stock ownership resulting in a request for representation on the directorate. Such representative may be a person of capacity and initiative or a mere dummy, but the desired interlocking is effective in either case. It therefore seems proper to widen our definition so as to bring under our consideration, not only the individuals with large interests in associated corporations, but their representatives as well. Finally, for any adequate treatment of the question it is necessary to include not only directors of corporations but also officers, for many of the problems of interlocking now occupying attention arise out of situations with which directors of a corporation as such have had little to do.

Confining our attention to the problem of interlocking as it concerns the railways, our discussion falls naturally into four divisions, according to the purpose in mind in the creation of the interlocking relationship: (1) interlocking for financial or credit purposes; (2) interlocking for industrial and commercial purposes, of which the principal one is the purchase of supplies; (3) interlocking for the purpose of railway construction and operation; (4) interlocking to restrain competition.

Let us consider these in order. Close association of railways with banks or other credit institutions first demands consideration. Such relationships have grown up naturally through the need for new capital constantly imposed upon an expanding railway system. Some railways have been fortunate enough to possess a relatively stable body of stockholders whose confidence in the management is so complete that new funds can be raised by direct appeal of the management to the stockholders without the intervention of outside financial interests. But these cases have thus far been rare in American railway finance. When the policy calls for the raising of funds by the issuance of bonds rather than stock, the appeal is to a wider and to an anonymous public rather than to a corporation's own stockholders. Frequently the appeal must be to a class of investors situated in another section of the country or even in a foreign country. Most railways have not the technical organization nor the established market necessary to handle their issues easily, and usually it is found that in spite of the often exorbitantly high

commissions which the bankers exact for their services, the net result is more satisfactory than that secured through the railway's own efforts. To the extent that this is the case, the bankers are performing a service of genuine economic value, and it must be concluded that under present conditions such service cannot readily be dispensed with.

Assuming this service as a necessity, the next step is for the banker to seek representation upon the railway board. His house has made itself responsible for a large issue of securities. It appeals to the investing public, not technically guaranteeing the issue, but practically doing so because of solicitude that its reputation for the handling of high-grade securities shall not be impaired. It seeks therefore to protect its own standing, and at the same time to make the securities more attractive to its customers, by demanding a place on the board of directors from which it can follow in detail the employment of the funds secured through its assistance. Large investors like life insurance companies, savings banks, fire insurance companies, guaranty companies, trust companies, demand as a prerequisite to purchase of securities that the underwriting house shall be represented on the board. The railway's credit—its ability to sell its issues—is dependent frequently upon the presence on its directorate of this representative. However, the banker is not in the position solely of a spectator or a detective. His expert advice is sought and usually followed. Often he is in a position where he can stipulate conditions under which alone he will undertake to provide the funds required, and such stipulations are frequently of immense influence in furthering efficient railway management. A recent example is found in the furnishing of money to the Chesapeake and Ohio Railway Co. by Kuhn, Loeb & Co. under a stipulation that the road must put back into its property each year a certain amount of its earnings. Instances might be multiplied in which railway corporations have been saved from disaster and set upon their feet through the aid of those who have furnished the funds, and who have stipulated in connection therewith that in order to insure their knowledge of all transactions, and to give them a position from which they might bring their influence to bear, they should be granted representation on

the railway board. The most concise justification of this attitude is found in the testimony given before the House Judiciary Committee on Trust Legislation in March by Mr. Loree, president of the Delaware and Hudson Co. Few men in New York City can speak with greater authority than he on these questions.

> The necessarily intimate relation between the banker and the seeker for accommodation is not changed when the latter ceases to be an individual or partnership and becomes a corporation. Precise and detailed disclosures concerning the affairs of the borrower are the recognized prerequisite of an application for credit, and constant information on the part of the banker is the desideratum when the applications for credit frequently occur. The simplest and most natural provision to meet this necessity is representation of the banker on the corporate board.[1]

Of course it must be admitted that the power of the banker may be misused to his own private advantage. The power is there—the power to refuse funds—the power that comes from command of enormous sources of capital, the prestige gained by years of successful experience. Men who have attained such a position have the personal qualities that give them naturally a commanding place in any council of business men. When such men dominate the policy of a railway and the results are disastrous, it is exceedingly difficult fairly to fix the responsibility and assess the blame. The line between good faith and good judgment or between personal ambition that amounts to breach of trust, and a misplaced optimism concerning the outcome of a specific policy, is a very difficult line to draw. Although praise and blame cannot be assigned with any precision between Mr. Morgan and Mr. Mellen in the unfortunate New Haven situation, it is the prevailing opinion of the New England public that it has not been benefited greatly by the presence on the New Haven board of the distinguished banker member. Generally speaking, however, the powerful banking interests have thrown their influence in the direction of railway efficiency and the public advantage. If our judgment as to the desirability of the relationship of railways and credit institutions is to be determined solely by results, we must conclude that the balance swings heavily in favor of the continuance of the present policy.

[1] *Hearings of the Committee on Judiciary*, H.R., 63d Cong., 2d sess., p. 1071.

However, opposition to the close association of financial houses and railways has not sprung from any such favorable relationships as we have here described. It grows rather out of the concentration and monopolization of credit. A powerful banking house which has identified its interests with that of one railway system is in position, because of its direct influence on the railway and its close affiliation with all other sources of credit, seriously to hamper if not altogether to prevent the securing of credit by a rival interest. This power over credit is not confined to one city or to one section of the country, but it reaches every section and even extends beyond national boundaries into the foreign sources of investment funds. Local or small enterprises requiring only moderate underwriting are frequently financed independently, but it is an acknowledged fact testified to by the large bankers themselves that with rare exceptions issues of securities in large amounts, except when taken up by the stockholders, must receive at least the tacit approval of the big financial group. Participation by the smaller banking houses in future underwritings depends upon loyalty to the syndicate in whatever enterprises are now being offered. The little fellows are inclined to respect a suggestion not to assist an enterprise of a character likely to interfere with undertakings already financed by the large interests. This informal but none the less effective network of alliances tends to destroy the competitive market for capital, and to restrict the railways to one source of credit. There does not appear to be any serious competition among the large bankers, but rather an understanding in the nature of a division of the field. A railway obtains the services of a single banking house which acts as its fiscal agent, underwrites its securities, receives its deposits, and has a representative on the railway's board of directors. When the railway becomes involved in financial difficulties, the same banking house organizes protective committees, devises reorganization schemes, and creates voting trusts. As Mr. Brandeis has put it, it adds to its duty as midwife also that of undertaker.

Is this relationship potentially dangerous for the railways and the public? The late Mr. Morgan, in his illuminating testimony in the money trust investigation, took the position that the situation

might be dangerous in the hands of the wrong men, but he clearly implied that there had been no bad results thus far and there were not likely to be in the future with a continuance of the present leadership. His argument reminds one of the young lady who "when she was good was very, very good, and when she was bad she was horrid." Yet this view is that of most of the financial leaders who appeared before the Pujo Committee. The following, for example, is from the testimony of Mr. James J. Hill:

Mr. Untermyer: Do you think the law should forbid or permit the same men to be directors in competing companies?

Mr. Hill: The effect of that would in my judgment depend upon the character of the man, the individual. I can understand possibly I might not want a competitor in a bank sitting at the bank board with me. I might not want him, but he might be the best director, and as good as I am. If he obeys the law, and regards his oath, he might be—

Mr. Untermyer (interrupting): Do you not understand that in passing laws you cannot have regard to the character of the men who are to act under them? Now, Mr. Hill, I am trying to find out from you whether you think the law should or should not forbid the same men being directors in competing companies? Have you any view on that?

Mr. Hill: My view is that in trying to do good you are liable to do harm; you might not necessarily do harm and you might not necessarily do good; but it depends on the individual man. All acts are personal things, and the mind and conscience of that individual man is what is going to govern his actions.[1]

Mr. Davison and Mr. Schiff both opposed the policy of concentration through interlocking at the point where the representative of the two interests might wield a dominating influence, but they found it difficult to fix that point.

Mr. Baker who took the position that safety lies in the personnel of the men, that in good hands interlocking could not do any harm, but in bad hands would be very bad, concluded nevertheless that the movement of concentration had gone about far enough. And Mr. George M. Reynolds of Chicago thus frankly expressed himself: "I am inclined to think that the concentration, having gone to the extent it has, does constitute a menace." And again, "I think a more wide distribution of the power of credit . . . . would

[1] *Hearings of the Committee to Investigate the Concentration of Control of Money and Credit.* (Pujo Committee), 62d Cong., 3d sess.

really be better in the long run." When asked the direct question, "Do you approve of the identity of directors or interlocking directorates in potentially competing institutions?" he replied, "Personally I do not believe that is the best policy."

It should be kept in mind that there is no evidence on record that this power has been used oppressively otherwise than in the rate of commission charged. Many of the bankers insist that the monopolization of credit is a physical impossibility. Even the Pujo Committee which displayed at times a childish prejudice against Wall Street and all its works was compelled, after an exhaustive investigation, to make the following admission:[1]

> It may be that this recently concentrated money power so far has not been abused otherwise than in the possible exaction of excessive profits through absence of competition. Whilst no evidence of abuse has come to the attention of the Committee from impartial sources, neither has there been adequate proof or opportunity for proof on the subject.

Yet it is known of all men that there does exist a well-defined community and even identity of interest among the financial leaders which extends into other fields of industrial activity than banking; that these financial interests are bound together through stock-holdings, interlocking directorates, voting trusts, and other devices; and that there is a concentration of credit in comparatively few hands.

If the conclusions thus far established are sound, it becomes clear that the real evil resulting from the interlocking of railways and credit houses, if any evil exists, arises primarily out of the relation of credit institutions to each other, rather than out of their relation to the railways through representation on railway boards. Were this interlocking of railways and banks to be wholly prohibited without any alteration in the organization of the credit market, I am unable to see how the situation would be changed materially. The tendency on the part of the bankers would still be to follow the law of "banking ethics" and divide the field; a railway would still employ a single banking house as its fiscal agent, and this banking house would still exercise a powerful influence

[1] *Report of the Committee to Investigate the Concentration of Control of Money and Credit*, 62d Cong., 3d sess., p. 133.

in determining the policy of the railway. At the same time the railway would be deprived of the presence on its board of a financial expert whose experience might be drawn upon in the detail of management day by day.

As Mr. Reynolds has admitted, the menace is in the concentration of credit. Such power may not thus far have been misused. But as the Pujo Committee has said, "whenever the incentive is at hand, the machinery is ready."[1] Those who have the public welfare at heart have no right to assume that such power will never be used to the personal interest of the bankers themselves and to the injury of the public. While I have no great enthusiasm for the popular pastime of rushing to Washington for a statute whenever the economic machinery fails to run smoothly, I am in sympathy with those who are studying the problem of the restoration of an open competitive market for capital.

However, this is a problem of extraordinary difficulty, and I do not myself see the way at present to its solution. I am aware that Congress has enacted legislation with the purpose of destroying this concentration of credit, and that many look upon the Clayton act, so far as it touches our problem, as a distinct step in advance. Personally I am skeptical as to its efficacy in its present form. The opportunities for evasion are too numerous. However, it can be laid down as a general rule that all statutory enactment which really endures is a product of successive increments of legislation—the result of experimental tests and the knowledge that is gained by experience. It is no argument against the interlocking provisions of the Clayton act that they do not solve the problem and that they can be evaded readily. Such an attitude of timidity and pessimism assumed twenty-five years ago would never have given us our present air-tight Interstate Commerce act. It may well be, however, that no relief can be found short of the radical step of employing government credit in aid of public-service industries. So vital is the necessity of the service to the people that the time may come when government loans to transportation corporations will appear to be a logical and natural step. But this is a digression.

[1] *Report of the Committee to Investigate the Concentration of Control of Money and Credit*, 62d Cong., 3d sess., p. 139.

Once this free market for capital is assured, the question again arises, Shall the railway board of directors contain banker members? Obviously the only purpose that the railway could then have in admitting bankers to its directorate would be the opportunity to utilize their experience in the direct management of the property. Quite as obviously the principal motive of the banker in accepting membership on a railway board would be to represent the underwriters and to act as fiscal agent. But with the capital market competitive, I can find no serious objection to such relationship. Even under present conditions the banker in the majority of cases respects his trust, refuses to vote on questions involving his personal interest, and performs loyally his service to the railway; but his mere presence on the board as the embodiment of the railway's only source of credit may be sufficient to control the situation in his behoof. However, with a free credit market, the dominating position of the banker largely disappears and he becomes what he ought to be, an expert adviser on financial matters. It may be asked why, if the banker is now to confine his activities to what Mr. Loree has called the "necessarily intimate relation between the banker and the seeker for accommodation," this cannot be accomplished in the same manner as in unincorporated businesses without putting the banker on the directorate. In reply attention may be called to the fact that even in the case of unincorporated businesses, the credit departments of the large banks are virtually in the position of directors, so intimate and comprehensive is their influence and advice. But more than this the business of a railroad is so complex and extensive, its activities are so multifarious, that an intimacy with its affairs sufficient to make the banker's counsel of value would be impossible except by actual presence on the directorate.

Under these changed conditions of credit, I can see greater opportunity for the utilization of the service of expert bankers in railway management. Directorships which have been monopolized in the hands of a few banker specialists in railway securities should then be more widely distributed. It is quite impossible to believe that expert banking talent available for this service is as rare as the present situation would suggest, in which the abilities of a relatively

few men are made to do duty in dozens of corporations. This absurd situation springs not from a scarcity of talent but from the narrow market for credit. A liberation of that market would bring latent ability from its hiding-places, and by the infusion of new blood would stimulate the management of our railway enterprises. It would open this field of activity to men "who have been obliged to serve when their abilities entitled them to direct."

The second class of interlocking relationships, that of railways with other industries, has varied manifestations, and is effected through varied forms of relationship. There may be a simple union accomplished through common directors on the boards of the railway and of the industry concerned, without any considerable joint ownership of securities; or some large stock-holding interest in the railway may own in part or in whole an industry whose product is essential to railway operation. This product may be a commodity in the narrower sense, such as iron and steel, oil, coal, lumber, patented equipment devices, and the like. Here the object of the affiliation may be either preferred rates and service in the shipment of goods to market, or it may be the railway's custom, sometimes at prices higher than the competitive price.

The Stanley Committee showed that the small group of men which controls the United States Steel Corporation, itself an owner of important railways, are directors in twenty-nine railway systems having 126,000 miles of line—more than half the railway mileage of the United States. The Steel Corporation is one of the largest shippers on these railways and the railways in turn are its most important customers.

Again the commodity that forms the connecting link between the railway and another business may be some service without which the operation of the railway is impossible. This is illustrated by the ownership at one time by a wealthy family group of a bridge on a railway's right of way for the use of which they were able to exact an excessive toll. Again close relations between express companies and railways have resulted in a modification of contracts between the two that has not always been to the public interest.

One of the early instances of this relationship came with the appearance of the "fast-freight lines." Directors of railways would

buy stock in the fast-freight company and then "give this company a contract which enriched it (and them) at the expense of the stockholders whose interests were intrusted to their charge."[1] The co-operative fast-freight line which succeeded this system was devised to escape these abuses. As Mr. Hadley says, "It avoids all stealing because there is nothing to steal."

Perhaps the most insidious manifestation of this form of interlocking is found in the relation of officers and employees of railways to supply houses. Stock has been taken, sometimes thoughtlessly, in equipment manufacturing concerns or in mining or lumber companies, which afterward have become solicitors for the business of the railway. In some cases coal companies, equipment companies, and the like have been organized by railway officers with no other apparent object than to make use of the influential positions of these officers in the railway organization for their own personal advantage. Sometimes they have attempted to cover their tracks by putting the outside business in the hands of relatives or friends. The exposures of a few years ago in the case of the Illinois Central show the extent to which such affiliations may, if unchecked, be carried.

Merely to describe this form of interlocking is a sufficient condemnation of it. It has no justification whatever, either from the public standpoint or from that of the stockholders. It is the duty of the executives of our railway systems to be eternally vigilant and to refuse to tolerate any compromise with this evil. There is no more justification for permitting a railway official to own the stock of a car company than there is for allowing a member of the Interstate Commerce Commission to own the stock of a railway, and the latter practice is forbidden by statute. It means the introduction of dry rot into the organization and sooner or later complete and demoralizing infection. The public knows only too little the extent to which this insidious disease has destroyed the vitality of railways, and has brought some of the largest and apparently most prosperous ones to the verge of bankruptcy. There applies here what Mr. Brandeis calls the principle of undivided loyalty. We have not reached and never can attain to that state of perfectibility where we can serve successfully two masters.

[1] Hadley, *Railroad Transportation*, p. 88.

We have it on the best authority that we shall hold to the one and despise the other, and our adherence will follow invariably the direction of our personal advantage.

From the public standpoint such alliances must likewise be condemned unqualifiedly. They can mean nothing but higher rates and poorer service for they tend to an increase in the cost of operation. Moreover they create a distrust of corporation management which bars the way to that hearty co-operation between public and carriers essential to satisfactory railway operation. "Milking the railway" is a bucolic pastime which has no economic or social justification.

The third class of interlocking relationships which falls within our consideration is that arising from the demands of construction or operation. The laws of a state may require separate incorporation within its borders of a proposed extension of an existing line; or the earlier financing of the parent company may have involved such contractual relations, that it is neither expedient nor possible for the existing company to issue on its own account the securities which at the time the market is prepared to absorb. A separate corporation is created for construction purposes, and the same men serve on the board of the parent and the subsidiary. Usually the subsidiary corporation continues to live after the construction period has ended. The maze of interlocking corporations that makes up a great railway operating system is a mystery to the uninitiated, and because the intimate relationships thus formed are unfortunately sometimes employed to cover practices and policies that cannot endure the full light of publicity, all such alliances arouse suspicion among a large class of the public. Yet many of them are absolutely essential, most of them are harmless. They have grown up gradually as necessity compelled and are retained because of the legal technicalities that bar the way to a more complete unification, and because of the cautious conservatism of the legal mind which is inclined to let well enough alone.

Outright purchase of one road by another involving the surrender of the charter of the purchased road is a step complicated with much troublesome legal detail, and frequently may compel the sacrifice of certain charter privileges not possessed by the

absorbing road. Even when no such special privileges appear to be attached to the old charter, counsel prefer to follow the modern, conservative slogan of "safety first" and retain the grant against a time of need. A small and stubborn minority, seeking its own selfish advantage and wishing to be bought off, may block the plan for a complete merger. State statutes, charter limitations, financial expediency, any one or all of these may compel the preservation intact of the corporation whose property it is desired to purchase. The simplest solution of these many difficulties has been the purchase of the stock of the corporation, usually through exchange of securities. Identity of directors and complete interlocking follows.

Some of our largest operating units have been welded together in this manner. The separate corporations have retained their identity, and the union has been effected through the purchase of their stock. Examples of this are the ownership of the Lake Shore and of the Michigan Central by the New York Central and of the lines west of Pittsburgh by the Pennsylvania Railroad through the Pennsylvania Company.

These parental relationships, so far as they relate to construction only, are in the nature of the case temporary. Those of a more lasting nature which bind an operating system together are, as a rule, in the interest of efficient railroading. They make for a more expeditious and a more generous service; they reduce the cost of operation and tend to lower rates. When this amalgamating movement has proceeded so far as to include under one operating system formerly independent and competing units, as in the absorption by the New York Central of both the Lake Shore and the Michigan Central, a different problem arises which will be considered under the fourth class of interlocking relations.

With the power in the hands of the Interstate Commerce Commission and many of the state commissions to control the accounting and examine the books of railway corporations, we may safely assume that the public interest will in nowise be prejudiced by the close relationship of parent railways and their subsidiary operating companies.

Restraint of competition is the actuating motive for interlocking relations of the fourth class. Care must be taken to distinguish

between an affiliation of roads which results in perfecting an operating system, and a close association of roads where no such object is apparent, but rather a restraint upon competition in some form. For lack of a better designation the first might be called longitudinal combination and the second parallel combination. The former would be illustrated by the New York Central's absorption of the Lake Shore property, the latter by the union of the Great Northern and Northern Pacific through the medium of the Northern Securities Company.[1]

Confining our attention to such affiliations as have the restraint of competition in mind, we ask ourselves what is their economic significance. But no categorical answer is forthcoming concerning a situation so complex. It depends upon the purpose in view and the method by which such purpose is effected. So far as the law is concerned, all forms of interlocking that restrain or tend to restrain competition would seem to be illegal. To be sure the decisions of the Supreme Court have not yet exhausted the possibilities of the Sherman act, but it seems clear from such decisions as have been rendered against the railroads, notably the recent Union Pacific merger case, that where restraint of competition can be proved, even though there is no evidence of injurious consequences to the public, the court will hold such a close relationship of railways to each other as an unreasonable restraint of trade. But we are concerned with economic rather than legal considerations, and here it is necessary to analyze somewhat the different forms of combination if we are to reach any sound conclusion.

At the one extreme there is the railway alliance formed solely for stock-jobbing purposes. There is no doubt that the unpopularity of railways may be traced in large measure to the manipulation of their securities and that if the able executives in charge of most of the systems were permitted to give their time exclusively to railway management and operation, and were unhampered by the restrictions placed upon them by selfish financial interests, the railway problem would assume much smaller proportions. I refer here not

[1] It will be recalled that the term interlocking directorate has been here stretched to include almost any form of relation in which the interests of one railway corporation have representation in an associated corporation.

to the banker class, but to a class with money and no principles—a class of which Wall Street in general would be glad to be rid. One of our economic brethren in a recent attack on railways, brought the charge against them that they had been fortune-builders; but the charge applies in large part only to the manipulator of railway securities, not to the permanent stockholder.

The corporate form of business organization, with its securities offered daily for sale on an unrestricted market, presents tempting opportunities to the unscrupulous manipulator to use his control of the railway for his own private advantage. For example, there is little evidence to show any interest in the development of an efficient railway service on the part of the buccaneers who organized the Rock Island Company. And while it may be possible to discern a justifiable economic purpose in the combination of the New Haven and the Boston and Maine railways through the Boston Holding Company, yet the means used, that of absolute monopoly of all forms of transportation in New England, cannot be defended. In the case of the Northern Securities Company, there was no evidence that results prejudicial to the public welfare had occurred, yet the merger contained such opportunities for the exercise of monopolistic power and had at the time relatively so little justification in the advantages to the public to be gained therefrom, that we must conclude that the Supreme Court's decision was not only good law, but good economics.

Interlocking devices that assist the railway wrecker and the financial juggler to accomplish their schemes are economically indefensible. In the employment of the holding company device to unite large systems, as in the case of the Northern Securities Company, or in the New York Central's ownership of the Lake Shore and the Michigan Central railroads, the burden of proof is clearly upon the shoulders of the railways to demonstrate the advantage to the public of such a relationship. As the court has insisted, such combinations by their necessary operation tend to destroy the motive for and to restrain competition.

A second form of relationship that would fall under this general head is that which results from stock purchases in another road to promote traffic alliances. Such alliances have in view questions

of service not rates. Examples of this would be the stock-holdings of the Pennsylvania in the New Haven. Whether or not such an interlocking is detrimental to the public interest is a matter of fact in each case. As a rule these interlockings have resulted in a more generous and efficient service, and in this respect they resemble the association of a parent road with its subsidiaries. Then there are those attenuated relationships, of which we have heard less lately than in former years, known as "community of interest." Under this plan representatives of two railways with common interests sit by invitation on one another's boards, for the purpose of harmonizing thus informally policies of common concern. In their origin, they had the specific purpose of stabilizing the rate situation. Such relationships must as in the preceding case, justify themselves by their results. There are many instances in which, should the law permit this form of consultation, they would be productive of public benefit. For example, much waste of passenger service results from the number of trains arriving at and leaving Chicago at the same hour on different railways, yet the railway officials dare not make agreements nor use the community of interest device for discussing a more economical arrangement because of the Sherman anti-trust sword hanging over their heads.

But in reaching a final conclusion as to the desirability from the public standpoint of such affiliations of parallel or potentially competing railways, I am compelled to look forward to what seems to me to be the inevitable outcome of the tendencies now at work. We have reached a point in the regulation of railways where competition in rates to any great degree is hardly probable. Economists have frequently demonstrated the undesirability of encouraging competition between industries subject to the law of increasing returns, and particularly between railways which have such enormous fixed plants in relation to the business done. Regulation has been substituted for competition as a public safeguard. But this principle of regulation has now been carried so far that the rate-fixing power has been virtually taken out of the hands of the railways and transferred to the Interstate Commerce Commission. Rates are rapidly becoming hardened at the maximum point fixed by the Commission, and competition, at least among parallel railways, has largely disappeared.

But the statement is frequently made that even though competition in rates is ended, railways should be prevented from agreements with one another in order that the public may enjoy the benefits of competitive service. But what, it may be asked, is an improvement in service but a reduction in rates, and why may not the practice of rebating be pursued even more successfully in this manner than by the more crude method of returning a part of the freight money?

In fact, in the knotty problems with which the Commission has wrestled such as elevator allowances, transit privileges, the absorption of switching charges, the spotting of cars, there is a clear recognition of the fact that these services are fundamentally problems of rates, that they must be adjusted by the regulating body, that they must be uniform and non-discriminatory, and that they must be filed as rates are filed for public inspection and criticism.

It is the pressure of competitive service that has driven the railroads into the impossible position which some of them now occupy where they are absorbing terminal services of such an expensive character that they are left with scarcely enough of the total rate to pay operating expenses; where the industrial plants are receiving from the railways a portion of the freight rate for the privilege of hauling their own cars about their own yards, with their own locomotives. Free storage, free loading and unloading, free collection and delivery, refrigerator service, milling in transit, prompt and abundant provision of cars, preferred service in matters of speed; all of these practices and many more have resulted in discriminations and have depleted the revenues of the roads. Reduced to their lowest terms these are all questions of rates, if not of rebates. From this tangle of inconsistent and unprofitable relations into which the railways have been forced by the pressure of competition, they can be extricated only with the aid of the Interstate Commerce Commission. The opposition aroused by their attempts recently to comply with the Commission's suggestions for the elimination of allowances to industrial railways demonstrates their helplessness.

There seems to me to be but one outcome. Before long the Commission will be compelled to regulate service quite as rigidly

as it does rates. All the power necessary to do so is already theirs by statute, and they have already in many individual cases made significant rulings that involve problems of service. It will only be necessary to recall the Illinois Central car distribution case which went to the Supreme Court and was used by that body as an occasion for establishing the final authority of the Commission in matters of administration.[1]

When that day comes, and it is not far in the future, that the Commission assumes as complete control of service as it has already done of rates, it will then in my judgment be of little or no public concern whether parallel and competing railways are or are not interlocked. That every evil of a monopoly character will then be done away with for good and all I do not assert. That would be placing too low an estimate on the ingenuity of the financial juggler. But the public advantages of co-operation on the part of large railway systems under the conditions here described so decidedly outweigh any remote disadvantages that there seems to me to be no justification for a prevention of interlocking relationships. Such close co-operation will work not to the restraining of trade unreasonably but rather to its liberation, for it will permit the execution of co-operative plans for relief in many situations that are now wastefully handled. It will permit the application of the principles of scientific economic railway operation to the railway system as a whole. It is a curious myopia that persists among the American people and demands competition between these great industries to the certain burdening of them ultimately with its inevitable costs. Yet with this prejudice against combination lodged in the breasts of the people, the movement of events as expressed in legislation has been steadily away from reliance upon the efficacy of competition and in the direction of more and more rigid regulation. That it will stop short of government ownership does not seem at all clear.

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[1] 215 U.S. 452.